PARTS OF THE ORIGINAL DOCUMENT

ARE OF POOR REPRODUCTIVE QUALITY

CERTAINES PARTIES DU DOCUMENT ORIGINAL

SONT DE PIÈTRE QUALITÉ DE REPRODUCTION

CONTENTS

Executive Reports 1

Marketing 5

Operations 8

Financials 15

Cover: Uranium-Bearing Rocks

The large blue-toned sample is extremely high-grade, containing about 60% uranium oxide (U_3O_8). Such extraordinary grades are only encountered underground. The smaller samples are low grade, averaging about 0.1% U_3O_8 and are commonly found in the sandstone cover or occasionally on the surface.

Saskatchewan Mining
Development Corporation
122 - 3rd Avenue North
Saskatoon, Saskatchewan
S7K 2H6 Telex 074-2864
Phone (306) 933-5000

Gold in Saskatchewan commonly occurs in quartz veins associated with pyrite. The gold is very finely disseminated and is not visible to the naked eye. This sample is from the Star Lake project.

Letter of Transmittal

The Honourable R.L. (Bob) Andrew, Minister Responsible for SMDC, (on the right) studies a total field magnetic map with Charles Roy, a senior staff geologist. Such maps trace the pattern of mineral occurrences in an area and are one of the many tools used in the continuing effort to detect economic orebodies.

March 28, 1987

To His Honour
The Honourable
Frederick W. Johnson
Lieutenant-Governor of
the Province of
Saskatchewan

Dear Sir:

I have the honour to transmit herewith the annual report of Saskatchewan Mining Development Corporation for the year ending December 31, 1986, including financial statements in the form approved by the Treasury Board and duly certified by the auditors of the Corporation.

Respectfully submitted,

Bob Andrew
Minister in charge of Saskatchewan
Mining Development Corporation

Chairman of the Board: "... Saskatchewan and Canada should support a free trade agreement with our largest trading partner, the United States of America, lest the door be closed to marketing of our natural resource products."

Last year I began my report by saying that the mood of pessimism was lifting from the world's uranium mining industry. Early events in 1986 tended to bear this out. The 100th nuclear power plant in the United States went into operation in Ohio. Seven more plants were later commissioned in that country. In Europe, France continued to demonstrate the efficiency of a standardized plant design. Average reactor construction time in that country is about six years, or less than half the time required in North America. Indeed, by the end of the first quarter of 1986, the industry seemed to be on a steady course toward growth and prosperity.

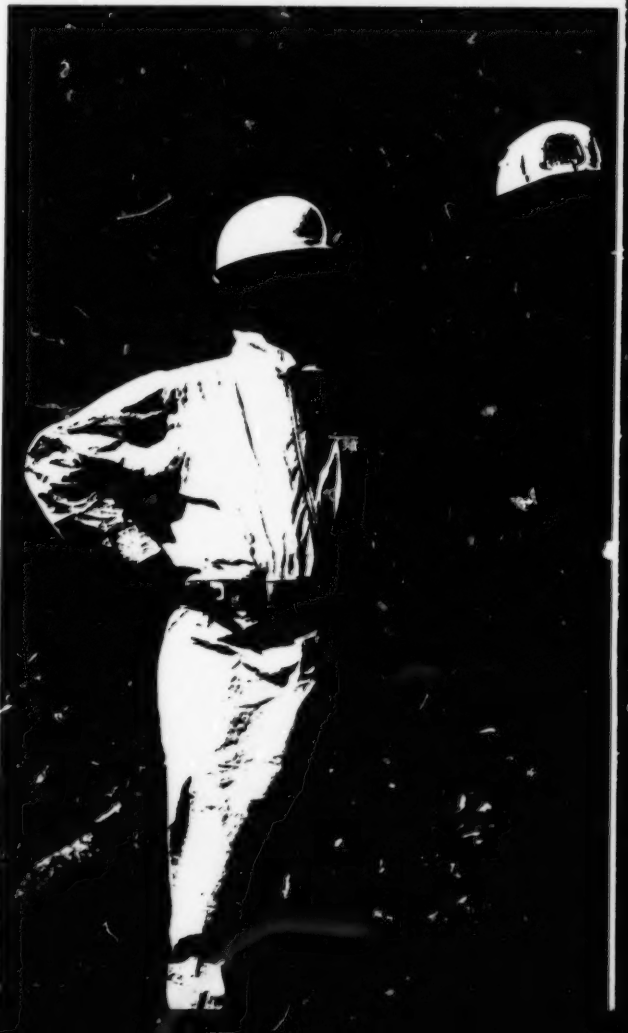
Then on April 26, 1986 at Chernobyl in the U.S.S.R., the industry experienced the most severe accident in its history. This incident immediately led to agreements for greater international co-operation. It is also evident that the accident will not cause any major changes to well-established reactor programs. SMDC joins others in our industry to remind the public that despite this tragic and preventable event, the nuclear power industry has an enviable safety record. Moreover, the environmental and human safeguards taken in the mining of uranium have resulted in a far safer record than the repetitive tragedies associated with the production of other fuels for electrical generation, such as coal mining, hydro dams and petroleum exploration and production. Clearly the balance of rational argument still shows that the use of uranium fuel is an efficient, safe, and economical method to generate electricity.

The largest market in the world for uranium fuel remains the United States where nearly 17% of all electricity in 1986 was generated by nuclear power. The growth of protectionism in that country is a concern to the Corporation and is another reason why Saskatchewan and Canada should support a "free trade" agreement lest the door be closed to marketing of our natural resource products — not only minerals, but our forest, fishery and water resources as well. These developments could help to bring prosperity to northern Saskatchewan where, presently, mining is the only stable industrial employer.

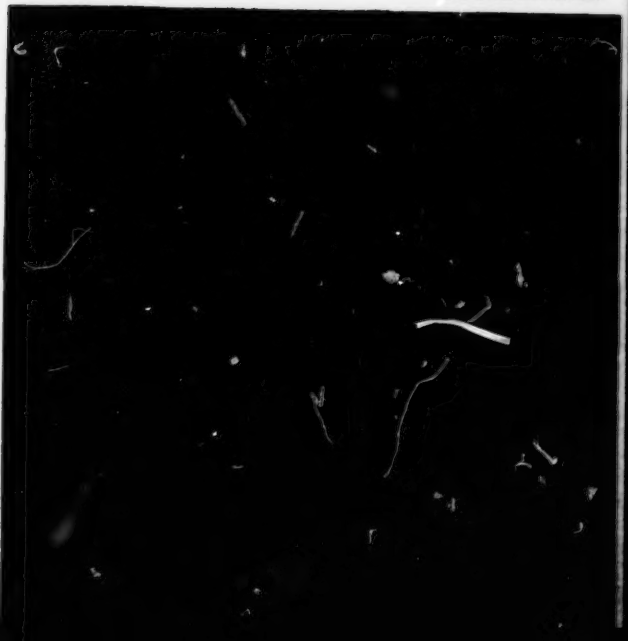
Despite its international focus, SMDC is first and foremost a Saskatchewan company. SMDC is a large part of the Saskatchewan uranium industry that last year contributed about $1 billion to Canada's gross domestic product. Directly and indirectly through our joint venture companies, we employ more than one thousand people who contribute a payroll of over $42 million to this province. A substantial portion of this impact is in northern Saskatchewan where SMDC has made a long term commitment demonstrated by such programs as Geo-Focus which gives northern high-school students work experience in our industry.

In late 1986 I was pleased to welcome to SMDC's Board of Directors the Honourable R.L. Andrew who was appointed Vice-Chairman. The Board joins me in expressing our confidence in the staff and management at SMDC who have proven that they can respond well to challenge and change.

E. W. Barootes
Chairman of the Board



Senator E.W. (Stan) Barootes, Chairman of the Board of SMDC, (on the left) pauses during a tour of the Star Lake site to discuss the project with Ken Frew, an assistant mine geologist.



This typical sample of sandstone is from the south wall of the Gaertner pit at the Key Lake mine. The pink tones are caused by iron staining. Sandstone forms a vast cap over the Athabasca Basin in northern Saskatchewan where it can vary in thickness from a few metres to more than a kilometre.

Marketing: "... We concluded four additional long-term sales agreements and extended the term and increased the quantities on other existing contracts."

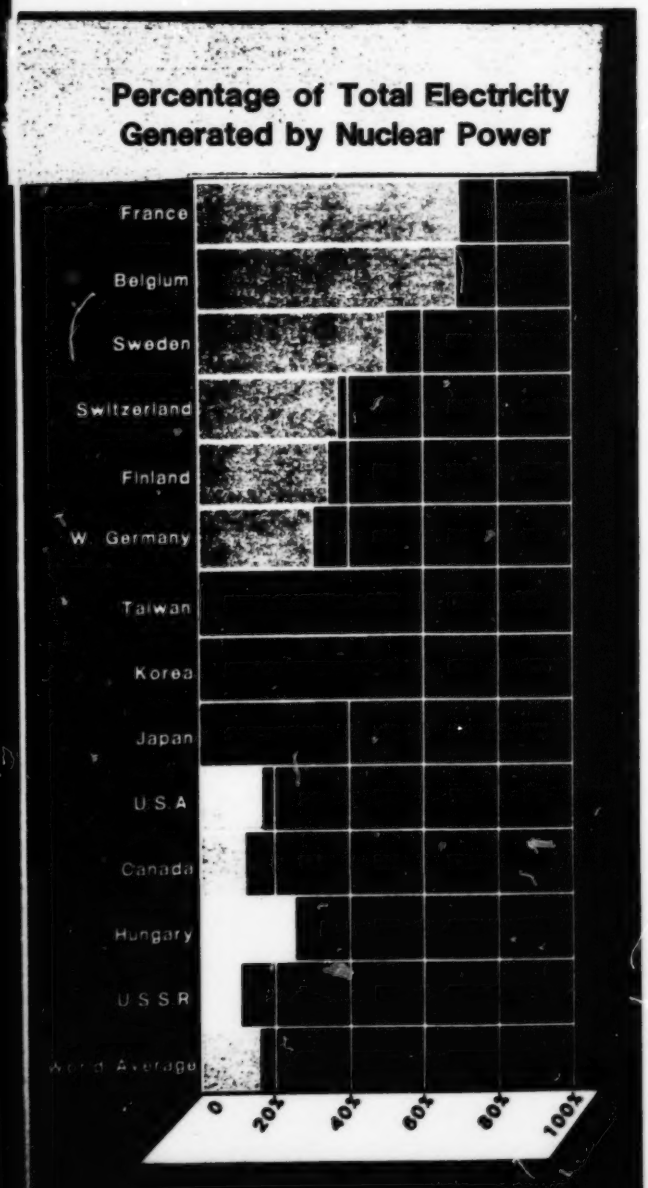
In 1986, SMDC continued its aggressive marketing program, combining long-term contracting with supplementary spot sales of uranium. Through the successful pursuit of this program, SMDC sold all of its Key Lake and Cluff Lake product this year.

Key Lake's large annual production, high grade reserves, and steady operating performance provide a secure basis for long-term contracting. SMDC's primary marketing objective is to substantially commit its 50% share of Key Lake production to such contracts. In 1986, we concluded four additional long-term sales agreements and extended the term and increased the quantities under existing contracts.

While recognizing that long-term uranium contracting is our primary objective, market forces and the need to maintain a degree of flexibility have resulted in some product being available for spot sales. Although the spot market was highly competitive in 1986, SMDC was able to sell all the product not delivered under long-term contracts. Because the Corporation goes into 1987 with our product substantially committed, we will be less active in the spot market. We will focus on our objectives of increasing long-term agreements from 1988 to the turn of the century.

Last year, we also delivered over one million pounds of U_3O_8 to complete the repayment of uranium borrowed in 1982 and 1983 under two loan agreements. These product borrowings had allowed SMDC an earlier penetration of world markets and contributed to financing the development of the Key Lake mine. A similar approach was implemented in 1986 to finance the development of SMDC's Star Lake gold mine.

Another important uranium marketing objective is diversification of sales. SMDC's customers are electric utilities in North America, Western Europe and the Far East. SMDC has successfully contracted long-term supply arrangements providing for about an equal level of



This chart represents a selected sample of the nuclear generation programs throughout the world. Europe has the most significant commitment to nuclear power, followed by the Far East.

Energy Equivalent Chart

SMDC's 1986 U_3O_8 Production

6.7 million lbs
U_3O_8

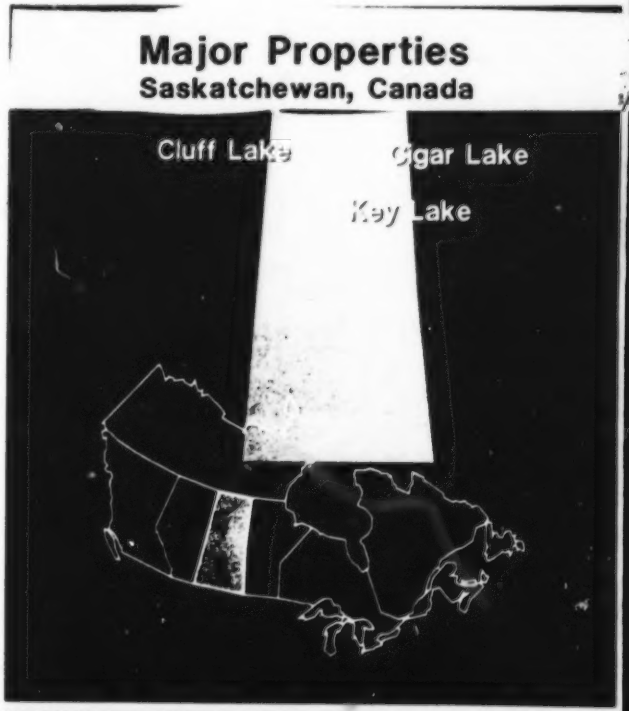
sales in each of these regions. In the short term, the United States will remain the most active because its inventories, as well as its current level of contractual commitments, are substantially lower than those in Europe and the Far East.

Spot market prices hovered around $17.00 US during the latter half of 1986, and are expected to improve during 1987; however, other factors are involved. On a global basis, consumption is rising as new nuclear power plants are brought into service. In 1986, for the second consecutive year, consumption exceeded production. This has the positive result of reducing the excessive utility inventories which have accumulated during the late 1970's and early 1980's. We expect this trend to continue through to the end of the 1980's by which time production and consumption should be in balance.

These gains could be offset by legislative and judicial actions in the United States to restrict the import of uranium. Since the final removal of import restrictions in 1984, the United States has been operating in a free trade environment. Faced with market realities, many of the less efficient mines in the United States have had to close down. However, some new, more efficient U.S. producers have emerged and demonstrated their competitiveness in the world market.

Should protectionist measures by the United States return, SMDC and other world uranium producers will be challenged to maintain current levels of productivity and profitability. We will continue to take advantage of opportunities as they develop in an uncertain market environment. Although we are unable to control protectionist legislation, we are nevertheless taking an active stance against it. With other producers, we believe that a free and competitive market for uranium and all fuel cycle activities is in everyone's best interests, especially the consumer.

SMDC's major uranium projects encircle the Athabasca Sandstone Basin which contains the world's richest known reserves of uranium.



6.7 million lbs. U_3O_8

- — fuels 16.75 - 1000 MWe reactors or provides 16,750 MWe

OR

- — provides same fuel as 221 million barrels of oil, almost ½ Canada's 1986 crude oil production

OR

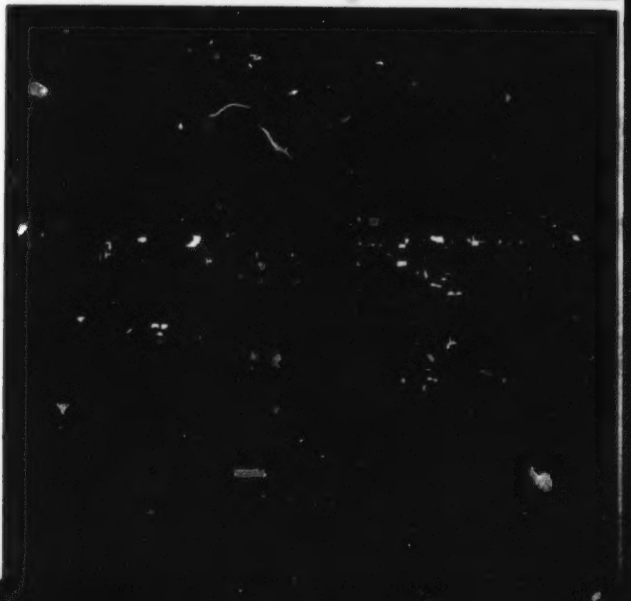
- — provides same fuel as 53.6 million tons of coal

OR

- — would fuel about 20% of Canada's electricity

OR

- — would fuel 86.6% of Swedish annual electrical generation (based on 1986 data)



Now connected to Tokyo by bullet train, Sendai is emerging as an international business center. Much of its electricity is supplied from the Onagawa nuclear power station operated by Tohoku Electric Power Corporation Ltd. which uses uranium fuel supplied by SMDC.

A beautiful example of the granite outcroppings that occur where the Canadian Shield is exposed at the surface. Such formations are commonly seen in northern Canada, extending from Quebec to Saskatchewan.

Mining & Engineering: "Ensuring that each project has the best people and materials available to do the job."

MINING AND ENGINEERING

The main objective of Mining and Engineering continues to be quality control: ensuring that each project has the best people and materials available to do the job. When these fundamentals are in place, SMDC leaves the details of daily operation to the operator. Results confirm that this operating strategy is sound. In 1986 Key Lake had record-breaking production levels; Cluff Mining registered steady improvement, and Star Lake advanced to production ahead of schedule and under budget.

Cost control and cost reduction are other important operating objectives. Careful monitoring procedures are in place to anticipate problem areas. SMDC also expects high standards at all projects for occupational health and safety, and for environmental protection.

Key Lake

Key Lake Mining Corporation (KLMC) is a joint venture operating company owned by SMDC (50%), Uranerz Exploration and Mining Limited (33 ⅓%) and Eldor Resources Limited (16 ⅔%).

Highlights:

- 1986 production increased to 12.59 million pounds U_3O_8. (4 841 tonnes U), or 105% of design capacity. This compares with 11.1 million pounds U_3O_8 (4 270 tonnes U) in 1985.
- Mineable reserves at December 31, 1986 are 161 million pounds U_3O_8 (62 000 tonnes U) contained in 3 520 000 tonnes of ore averaging 2.07% U_3O_8(1.76%U).

The world's largest producing uranium mine, Key Lake milled 248 530 tonnes of ore in 1986, with a mill feed grade of 2.31% U_3O_8 (1.96% U). Recovery was improved to 97.9%, from last year's recovery of 95.4%. The yellowcake product was a very pure 97.78% U_3O_8.

In the Gaertner pit, mining of the primary ore was completed and stripping of a final cobble ore pod was started. However, Gaertner ore from the stockpile will continue to be milled until 1989.

Development of the Deilmann orebody, the larger of the two at Key Lake, proceeded at an excellent rate during 1986. Over 1.3 million bank cubic metres of waste stripping was completed, in preparation for mining. An evaluation is underway to assess the feasibility of mining some of the Deilmann ore zone by cheaper, more selective underground methods.

SMDC's objective of cost control was well met by modest plant modifications during 1986, which have improved plant throughput rates and reduced costs and maintenance downtime. Some further modifications are ongoing and will be completed in 1987.

Continued emphasis on occupational health and safety has helped reduce the number of time lost accidents for the third year in a row. In 1986 there were nine time lost accidents, compared with fourteen in

The Gaertner pit at the Key Lake mine where a record-breaking 12.6 million pounds of U_3O_8 was produced in 1986.

1985, and eighteen in 1984. A new collective agreement has been ratified by the union membership and is effective until 1990. This should contribute to continued high productivity at the site.

Cluff Mining

Cluff Mining is owned by Amok Ltd./Ltée. (80%) and SMDC (20%), with Amok as operator of the project. Highlights:

- 1986 production totalled 2.17 million pounds U_3O_8 (833.7 tonnes U), equal to 1985 production.
- Mineable reserves at December 31, 1986 are 36 million pounds U_3O_8 (13 900 tonnes U) contained in 2 560 000 tonnes of ore averaging 0.64% U_3O_8 (0.54% U).

Approvals were received to proceed with the construction of a plant to reprocess the leach tailings from Phase I of the operation. This system will recover gold and additional uranium values and will make it possible for the operator to safely dispose of the tailings in the existing waste management area. The plant is scheduled to commence operations in March 1987.

Cigar Lake

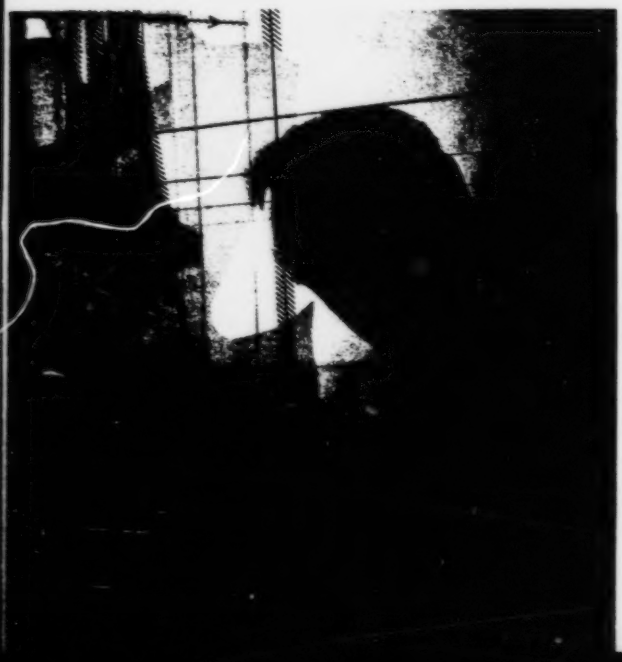
Now in the pre-development stage, the Cigar Lake project in northern Saskatchewan is a joint venture between SMDC (50.75%), Cogema Canada Ltd. (33.625%), Idemitsu Uranium Exploration Canada Ltd. (11.875%) and Corona Grande Exploration Corporation (3.75%), a wholly owned subsidiary of Cogema Canada. The Cigar Lake Mining Corporation was formed in 1985 to bring these reserves to commercial production in the early 1990's.

The Cigar Lake project is by far the largest high-grade uranium deposit in the world. Drill indicated reserves are estimated at 285 million pounds U_3O_8 (110 000 tonnes U) in ore grading 14.0% U_3O_8 in the main zone, and a further 100 million pounds U_3O_8 (38 500 tonnes U) grading 4.5% inferred in the western extension. The Cigar Lake orebody lies at a depth of some 430 metres and is hosted in weak rocks with a high clay content. Important technical issues which have been addressed in the predevelopment stage include groundwater, rock properties, and radiation protection.

Approval for construction of a temporary access road was received and preparations for a test mine continued on schedule throughout 1986. The focus of preliminary engineering for the test mining facilities included mining concepts, radiation protection, water treatment and environmental assessment.

A project proposal has been submitted to the Saskatchewan Department of the Environment and work has begun on the preparation of the Environmental Impact Statement and underground exploration permit. We are targeting to receive all necessary approvals to allow shaft sinking to start in late 1987. Initial estimates indicate $50 million may be spent on the test mine in the period 1987 to 1989.

While the start of commercial operations will be market driven, current estimates foresee construction of a 12 million pounds U_3O_8 (4 600 tonnes U) per year mill during the period of 1990 to 1993.



George Peebles, General Manager of the Cigar Lake Mining Corporation, examines a cross-section of the richest zone of the Cigar Lake orebody where grades can range as high as 30% U_3O_8.

Star Lake

The Star Lake gold project is operated by SMDC (50%) in partnership with Uranerz Exploration & Mining Limited and Starrex Mining Corporation Ltd.

The only gold mine in the province, Star Lake, reached a significant milestone on January 2, 1987 with the pouring of the first test gold bar.

Mineable reserves blocked out to the 420 level at December 31, 1986 were 150 800 tonnes grading 0.42 oz/ton (14.4 grams/tonne), and containing approximately 70,000 ounces (2 170 kg) of gold.

In early 1986, work on the Star Lake project focused on the completion of the first stage of the underground decline. This entry provided access to the orebody, which allowed for reserve verification and bulk sampling. Results confirmed the decision to proceed.

In the latter half of the year, all remaining mine development and

stope preparation was completed. Approvals to operate were obtained in November 1986, and soon after mining of the first shrinkage stope was completed. The mill, camp and tailings system were also substantially in place by this time.

Mill commissioning was in progress from November 15, 1986 until year end. Approximately 2 800 tonnes of low grade ore were milled during December, and the first trial doré bullion bar was poured January 2, 1987. The mine's commercial production schedule is 220 tons per day (200 tonnes per day).

SMDC's commitment to cost control helped bring the project in under the $13 million budget. An aggressive exploration program is planned for 1987 which could extend the reserve base of the Star Lake project. Drilling will be concentrated on the 21 Zone below the 420 level, as well as on the Rush Zone and other structures on the property.

Other Developments

In keeping with SMDC's objective of diversification, studies continued throughout 1986 involving gold, yttrium, magnesium, graphite and cement.

Other studies done during the year included those done by the Uranium and Precious Metal Study Group, which completed work on the impact of cyanide and arsenic on the environment of northern Saskatchewan. The group also carried out a terrain classification study, which involved satellite-derived remote sensing data for the area around the Star Lake project.

The compressors supply all the compressed air required in the Key Lake plant for agitation of tanks and powering of air-operated equipment.

Barium chloride is metered into the mill effluent in order to remove radium.

Exploration: "Ensuring that the Corporation has sufficient low-cost reserves to maintain or improve our position in world markets . . ."

EXPLORATION BRANCH

The establishment of an adequate reserve base is, and will continue to be, the main priority of SMDC's exploration program. This objective will ensure that the Corporation has sufficient low-cost reserves, particularly in uranium and gold, to maintain or improve our position in world markets as the deposits currently in production are gradually depleted. Given the Corporation's strong uranium reserve position, this strategy extends several decades into the future.

SMDC pursued this objective in 1986 by continuing our traditionally high level of uranium exploration and also expanding the Corporation's gold exploration activity. Most of the uranium activity is focused on the eastern edge of the Athabasca Sandstone Basin, extending northward under sandstone cover between Key Lake and Cigar Lake. Uranium exploration expenditures continued at about $15 million and precious and base metals exploration increased from $4.4 million in 1985 to $8.7 million in 1986.

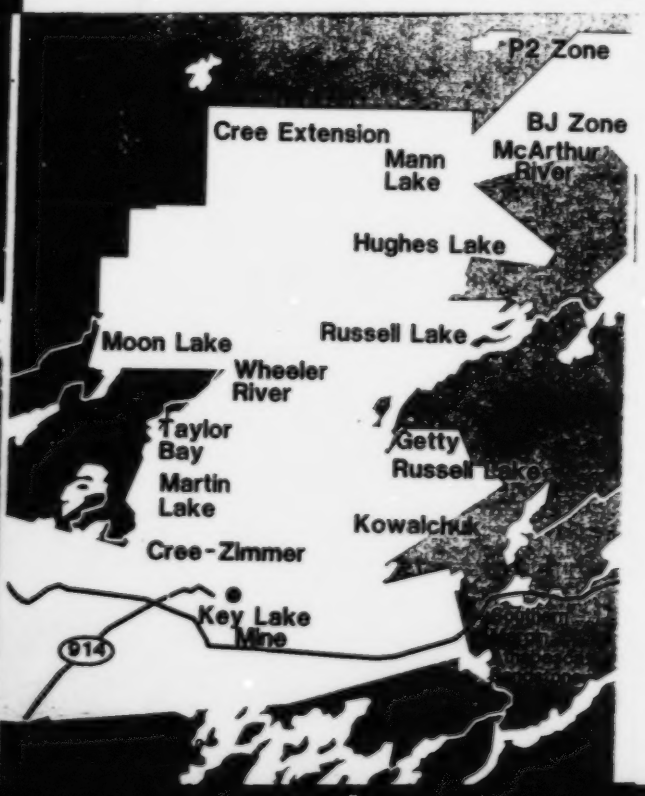
Another exploration objective involves the cost effective management of the Corporation's exploration dollars. Through joint venture arrangements, SMDC has sought to maximize the odds of exploration success while maintaining an interest in significant land holdings at minimum cost. This strategy continued to be successful in 1986 when, through farmout arrangements and joint venture projects, the Corporation participated in a $24 million exploration program at a cost of approximately $5 million.

Exploration spearheaded the Corporation's drive towards greater commodity diversification. While gold continues to be the principle target of this program, SMDC also participated in two platinum projects, four polymetallic mineral projects, and one industrial minerals project in 1986.

Uranium Projects

SMDC continued its strong uranium program, participating in some projects and operating others. Activity was concentrated in areas close to existing and planned mills in the Eastern Athabasca region and the Cluff Lake area in order to increase reserves in the vicinity of existing mills.

The major target of this exploration was graphite-associated deposits of the high-grade Key Lake and Cigar Lake type, which are closely associated with the unconformity beneath the Athabasca sandstone. Major projects in this category were located near Key Lake, in the Russell-Wheeler lakes area, north of Key Lake, and in the Waterbury-Close-Dawn lakes area, farther to the northeast. On the McArthur River project, a related, but somewhat different, type of uranium mineralization was investigated within sandstone above the unconformity. Other projects, particularly near Cluff Lake and at Eagle Point, also sought mineralization within pre-Athabasca basement rocks. Highlights from some of the advanced projects include:



Major Uranium Properties in the Key Lake Area.

McArthur River

Further drilling was carried out at the P2 location on the McArthur River project. Out of six holes completed, three had uranium mineralization, with the best intersections being 0.68% U_3O_8 over 16 m and 0.38% U_3O_8 over 8.5 m. This mineralization, which extends over a length of 500 m in sandstone, will see additional drilling in 1987. Joint venture partners are Uranerz Exploration and Mining Limited, Cogema Canada Limited, AGIP Canada Limited, and Interuranium Ltd.

Key Lake Area

During the year, further farmout agreements were concluded on four uranium projects located north of Key Lake. As a result, additional funding was obtained to allow renewed exploration on the Cree Extension, Hughes Lake, Mann Lake and Moon Lake projects, all of which are within hauling distance to the Key Lake mill.

Wheeler River

Drilling at Zone M on the Wheeler River project intersected mineralization at the pre-Athabasca unconformity which is at a depth of 350 to 400 m. Associated alteration features are similar to those around known high-grade uranium deposits elsewhere in Saskatchewan.

This project, located 35 kilometres northeast of Key Lake, has several conductive trends which are considered favourable for graphite-associated uranium deposits beneath sandstone cover from 350 to 500 m thick. The 1986 program, consisting of ground geophysical surveys and 4 266 m of diamond drilling, was part of a continuing program to assess the property. Other partners in the joint venture are Imperial Metals Corporation, AGIP Canada Ltd., and Denison Mines Limited.

Eagle North

SMDC holds a 1/3 interest in this project, which has entered the predevelopment stage based on better-than-anticipated results from both this project and the related development at Eagle South. Reserves at Eagle North are estimated at 58.4 million pounds U_3O_8 (22 450 tonnes U) at a grade of 2.07% U_3O_8 (1.76% U).

Dominique-Janine Area

Exploration in the Cluff Lake area, managed by Amok Ltd/Ltée., discovered additional uranium reserves in the Dominique-Janine area which will be quantified by further drilling in 1987. This is part of a continuing program seeking further low-cost reserves for the Cluff Lake mill.

Gold Projects

During 1986 SMDC continued to explore for gold in Saskatchewan concentrating mainly on the La Ronge greenstone belt and the Flin Flon domain. These areas favour successful development because they combine good exploration potential with proximity to roads and other infrastructure.

Compared to the major gold producing areas in Ontario and Quebec, these geologically-similar areas in Saskatchewan have been relatively neglected by exploration companies in the past. Systematic gold exploration in the last several years, however, has recognized that gold occurs in a variety of geological settings including quartz veins in granites; shear-related stockworks in volcanic, sedimentary and mafic intrusive rocks; and disseminated mineralization, with associated bonanza veins in felsic pyroclastic rocks. These are considered to be prime exploration environments where medium and large deposits may occur. The Corporation's gold activity is concentrated in the following areas:

La Ronge Greenstone Belt

SMDC's greatest concentration of gold exploration activity focused on a group of projects in the vicinity of the Star Lake mine. These include the Star Lake project and the adjacent David Lake and Blindman Lake projects, the latter of which is operated by Golden Rule Resources Ltd. While surface exploration and drilling on these properties in 1986 did not discover new economic reserves, sufficient encouragement was obtained to continue aggressive exploration on all three projects next year.

During 1986 SMDC formed a joint venture with Claude Resources Inc. and Shore Gold Fund Inc. to explore previously known gold mineralization on the Jojay Lake and Tamar properties.

A drilling program of 2 068 metres in 17 holes was completed on the Jojay zone, which is located seven kilometres north of the Star Lake mill. This program was designed to confirm mineralization previously drilled in the 1940's. Assay results from the SMDC program showed significant gold values in 14 out of 17 holes, ranging from 0.125 oz gold over 2.25 m to 0.322 oz gold over 6.7 m. The zone has been tested over a strike length of 200 m to a depth of 80 m. Further drilling is planned for 1987.

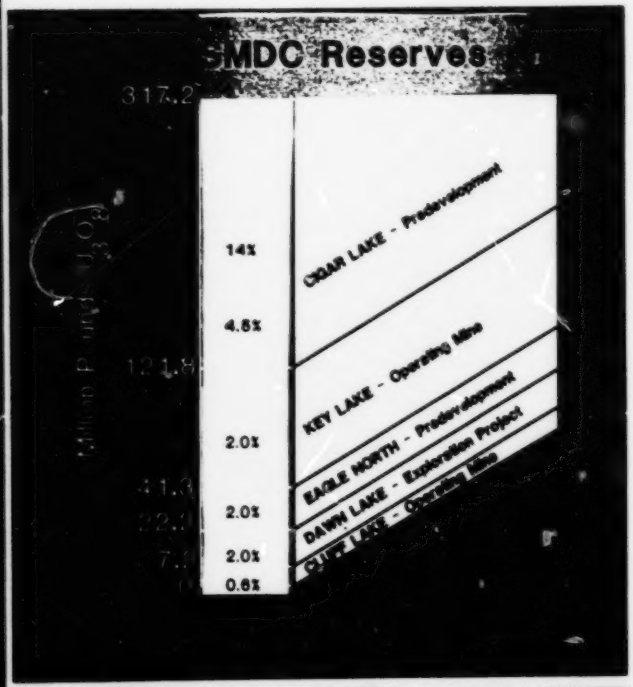
Diamond drilling on the Tamar project intersected subeconomic gold

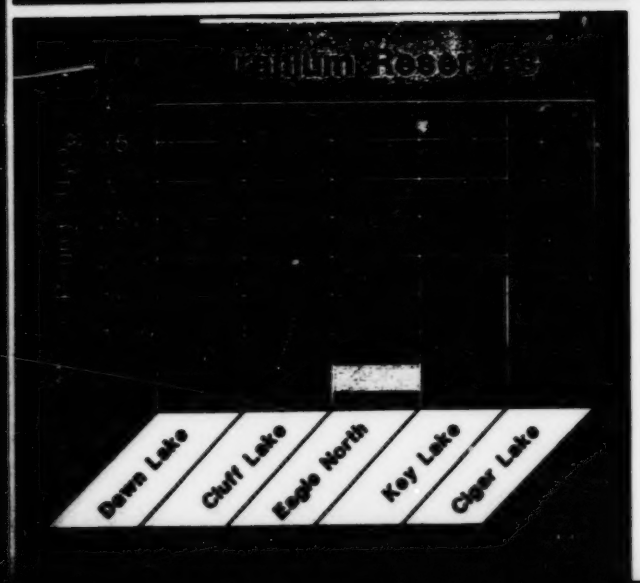
Major Gold Properties in the Star Lake Area.

mineralization in several drill holes completed in 1986. These results, together with surface exploration on the property, indicated a sizeable gold-bearing structure on which further exploration is planned in 1987.

SMDC is a partner in the Tower East project, along with Goldsil Resources Ltd. and Golden Rule Resources Ltd. Drilling continued in 1986 at the site, approximately 25 kilometres northeast of Star Lake. The purpose was to confirm and further delineate shallow mineralization previously estimated to contain 770 000 tonnes (850,000 tons) at an average grade of 0.13 oz gold per ton. This year's results outlined zones of higher grade within the broad envelope of mineralization, and based on these positive results, further drilling is planned for 1987.

Continued encouraging results were obtained from surface exploration and diamond drilling on the Preview Lake project, located within La Ronge Provincial Park, 40 kilometres northeast of the town of La Ronge. In the Pap Lake area, ten drill holes tested shear zones in dioritic rocks. Gold mineralization was intersected at all locations drilled. A 1987 drilling program will continue to test these zones. Surface exploration, including prospecting, mapping and geochemical surveys during the year has indicated other areas on this large property (12 731 hectares) that will warrant further examination in the coming year. Partners in the project are Uranerz Exploration and Mining Limited and Windarra Minerals Ltd.



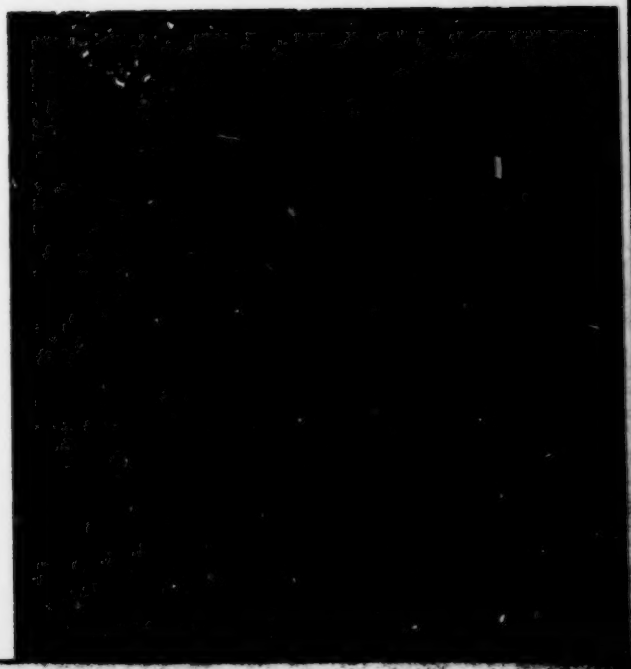


SMDC's high-quality uranium reserve base is among the best in the world. The Corporation is well-positioned to meet new market demands in the early nineties.

Flin Flon Domain

The major SMDC project in this region was the Amisk Lake project, an 18 600 hectare property located approximately 20 kilometres southwest of Flin Flon. In 1986, a major drilling program on the Laurel Lake gold zone on Missi Island included 18 drill holes (2 107 m) during the winter, followed by a summer program of 1 968 metres in 15 drill holes. This drilling confirmed a system of multiple gold- and silver-bearing mineralized zones extending over 450 metres. Intersections of potential ore grade mineralization over mineable widths occur over lengths of 100 to 150 metres at both ends of the system. Drilling is planned in 1987 to delineate further the Laurel Lake mineralization and investigate other parts of the property.

During the year, Husky Oil Operations Ltd. became a participant in this project and will earn a 50% interest by funding on-going exploration on the property. SMDC is operator of this joint venture and will own 50% interest after Husky completes its earning obligations.



This interesting pattern is the result of intense heat and pressure that has caused multiple foldings of the rock, a process begun about 3 billion years ago. This sample is found at the Amisk Lake project near Flin Flon.

Financials: "Net debt obligations of the Corporation were reduced by $45.3 million during 1986."

COMMENTARY

In order to achieve the Corporation's primary objective of improved profitability and greater return on investment, it is imperative that our heavy and abnormally high-cost debt be reduced. This has become a priority since the completion of the development and construction phase of the Corporation's two major producing facilities.

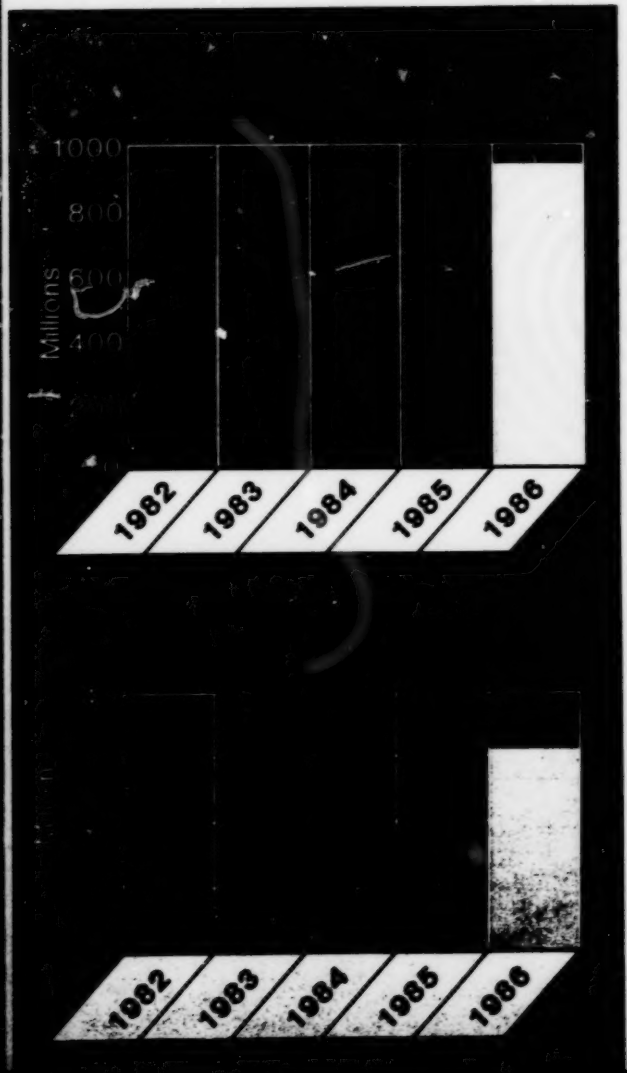
After capital expenditures and dividend payments, net debt obligations of the Corporation were reduced by $45.3 million during 1986. Net earnings for the year of $30.4 million are $12.4 million higher than last year's $18.0 million. Cashflows from operations were $109.2 million, an increase of 8% over the previous year. Interest payments of $68 million consumed 62% of these cashflows down from 75% in 1985.

The proportion of interest charged to earnings dropped from 73% in 1985 to 65% this year, as the Star Lake, Cigar Lake and Key Lake (Deilmann orebody) development projects attracted a greater portion of the total interest costs. Interest is capitalized on each of these projects until they achieve commercial production. Interest for the year includes $11.3 million (1985 - $13.7 million) to provide for possible foreign exchange losses as each long-term debt instrument matures.

As part of its debt management strategy, the Corporation continued to utilize interest rate swaps as a tool to reduce debt charges. These interest rate swaps, which have the effect of converting fixed rate debt into floating rate debt, reduced interest costs during the year by $5.2 million. During the year, U.S. $35 million of the Corporation's U.S. $175 million interest rate swap portfolio was reversed, providing a "locked-in gain" until their maturity.

As a longer-term defensive strategy, the Corporation undertook long-term borrowings through the Province of Saskatchewan during the year, namely a U.S. $35 million 8 1/2% note and a U.S. $25 million 7 1/2% note. These borrowings were undertaken to partially hedge against possible future increases in interest rates. The proceeds of these borrowings were used, in part, to pay down short-term borrowings with the balance held in short-term investments to apply to the U.S. $100 million debt which can be redeemed in the latter part of 1987.

For the fifth consecutive year, the Corporation maintained its tradition of paying a dividend to the Province of Saskatchewan. The 1986 dividend of $15 million is almost double that paid to the Province for each of the prior two years.



Over the past five years SMDC's assets have increased by nearly $300 million and net earnings are more than five times greater.

Outstanding Debt Obligations

	(Millions of dollars) 1986	1985
Long-Term Debt and Deferred Revenue	$587.9	$507.1
Bank Indebtedness	—	33.9
Current Portion of Long-Term Debt and Deferred Revenue	4.7	30.1
	592.6	571.1
Less Cash and Short-Term Investments	66.8	—
	$525.8	$571.1

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING IN THE ANNUAL REPORT

Management has prepared the financial statements of the Corporation in accordance with generally accepted accounting principles applied on a consistent basis. The financial data included elsewhere in this report is consistent with the financial statements and the underlying information from which these financial statements were prepared.

Management has the primary responsibility for the integrity and objectivity of the financial statements. To fulfill this responsibility, the Corporation maintains appropriate systems of internal controls, policies and procedures to provide reasonable assurance that assets are safeguarded and that the books and records reflect the authorized transactions of the Corporation.

Clarkson Gordon, the Corporation's external auditors, have examined the December 31, 1986 consolidated financial statements and their report follows.

The statements have been examined and approved by the Board of Directors.

On behalf of the Corporation.

Vice President
Finance and Administration

AUDITORS' REPORT

To the Members of
The Legislative Assembly,
Province of Saskatchewan

We have examined the consolidated statement of financial position of Saskatchewan Mining Development Corporation as at December 31, 1986 and the consolidated statements of operations and reinvested earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at December 31, 1986 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Clarkson Gordon

Saskatoon, Canada,
March 10, 1987,

Chartered Accountants

CONSOLIDATED STATEMENT OF OPERATIONS AND REINVESTED EARNINGS

Saskatchewan Mining Development Corporation
Year ended December 31, 1986

	(thousands of dollars)	
	1986	1985
Revenue:		
Sales of concentrates	$179,941	$174,553
Other	—	316
	179,941	174,869
Expenses:		
Operating	35,359	35,822
Depreciation and amortization	41,498	38,942
Provincial royalties and taxes	6,453	5,373
Selling and administrative	3,355	3,262
Exploration project areas written-off	7,450	3,675
Other	546	—
	94,661	87,074
Operating earnings	85,280	87,795
Interest expense (note 3)	54,888	69,746
Net earnings	30,392	18,049
Reinvested earnings, beginning of year	18,596	8,547
Deduct dividend	15,000	8,000
Reinvested earnings, end of year	$ 33,988	$ 18,596

(See accompanying notes)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Saskatchewan Mining Development Corporation
December 31, 1986

	(thousands of dollars) 1986	1985
Assets		
Current:		
Cash and short-term deposits	$ 66,818	$ —
Accounts receivable	17,594	21,533
Inventories (note 4)	15,492	14,539
Prepaid expenses	363	242
	100,267	36,314
Property, plant and equipment (note 5)	819,439	816,143
Deferred charges (note 6)	27,839	45,712
	$947,545	$898,169
Liabilities and Province's Equity		
Current:		
Bank indebtedness	$ —	$ 33,920
Accounts payable	12,519	10,793
Deferred revenue (note 7)	4,670	30,135
Dividend payable	15,000	8,000
Accrued interest on long-term debt	40,349	37,279
	72,538	120,127
Provision for restoration costs	3,234	2,494
Deferred revenue (note 7)	4,669	—
Long-term debt (note 9)	583,275	507,111
Total liabilities	663,716	629,732
Province of Saskatchewan's Equity:		
Advances (note 10)	249,841	249,841
Reinvested earnings	33,988	18,596
	283,829	268,437
	$947,545	$898,169

(See accompanying notes)

Approved by the Board of Directors

Director: E.W. Barootes

Director: J.H. Morrison

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

Saskatchewan Mining Development Corporation
Year ended December 31, 1986

	(thousands of dollars) 1986	1985
Sources of cash:		
Cash provided by operations		
Sales of concentrates	$148,978	$140,003
Operating, selling and administrative expenses	(37,974)	(37,888)
Provincial royalties and taxes	(6,453)	(5,373)
	104,551	96,742
Cash provided by (invested in) changes in non-cash working capital		
Accounts receivable	3,963	2,924
Inventories	(953)	547
Prepaid expenses	(121)	(131)
Accounts payable	1,726	675
	4,615	4,015
Total cash provided by operations	109,166	100,757
Other sources of cash		
Proceeds on disposal of fixed assets	120	1,030
Deferred revenue	9,339	—
Long-term debt	84,123	—
Interest revenue	1,105	709
Other income (expense)	(546)	316
	94,141	2,055
Total sources of cash	203,307	102,812
Uses of cash:		
Cash invested in property, plant and equipment	24,079	21,020
Cash committed to financing activities		
Repayment of long-term debt	—	65,000
Deferred financing costs	2,533	57
Interest	67,957	75,249
Dividend	8,000	7,600
	78,490	147,906
Total uses of cash	102,569	168,926
Increase (decrease) in cash	100,738	(66,114)
Cash (Deficiency), beginning of year	(33,920)	32,194
Cash (Deficiency), end of year	$ 66,818	$ (33,920)

Note: Cash includes short-term deposits and bank indebtedness.

(See accompanying notes)

Saskatchewan Mining Development Corporation
December 31, 1986

1. Accounting Policies

This summary of significant accounting policies is a description of the accounting methods and practices that have been used in the preparation of these consolidated financial statements.

Consolidation Principles

The consolidated financial statements include the accounts of the Corporation and its wholly-owned subsidiary SMD Mining Co. Ltd.

Joint Ventures

The Corporation's assets and liabilities relate primarily to its interest in the following joint ventures and partnership:

	Operator	Corporation's Interest
Uranium:		
Producing:		
Key Lake	Key Lake Mining Corporation	50%
Cluff Mining Partnership	Amok Ltd.	20%
Non-producing:		
Cigar Lake	Cigar Lake Mining Corporation	50.75%
Gold:		
Non-producing:		
Star Lake — construction substantially completed	Saskatchewan Mining Development Corporation	50%

In addition, the Corporation has interests in other joint ventures varying from 10% to 85%.

Interests in joint ventures and the partnership are accounted for by the proportionate consolidation method.

Inventories

Broken ore and concentrates are valued at the lower of production cost and estimated net realizable value. Supplies are valued at the lower of average cost and replacement value.

Production Facilities and Equipment and Depreciation

Production facilities and equipment are carried at cost and are depreciated by the unit of production method over the estimated economically recoverable ore reserves or by the straight line method if the estimated useful life of the asset is less than the estimated mine life.

Other facilities and equipment are carried at cost and are depreciated by the straight line method at rates varying from 10.0% to 33.3%.

Deferred Mineral Property Costs and Amortization

Each group of contiguous mineral properties is accounted for separately and is designated as a project area. All acquisition of mineral properties, exploration, development and other expenditures relating to each project area are deferred and carried at cost with the intention that they will be amortized by charges against earnings from future mining operations. At such time as it is deemed that a project area does not contain economically recoverable ore reserves the related deferred expenses are written off to earnings.

The decision to develop a producing mine property within a project area will be based on an assessment of the conditions prevailing at that time. No depreciation or amortization will be provided on such a property until commercial production commences. After a mine property has been brought into commercial production, any additional work thereon will be expensed as incurred, except for large development programs, which will be deferred and amortized over the related remaining reserves.

Deferred mineral property costs are amortized by the unit of production method based on the property's estimated economically recoverable ore reserves.

Capitalization of Interest

Interest is capitalized on expenditures related to construction or development projects. Capitalization is discontinued when the asset is ready for its intended use or development ceases.

Financing Costs

Premium, discount and issue costs of long-term debt are deferred and amortized over the term of the issues to which they relate. The amortization is included with interest.

Foreign Exchange Translation

Current assets, current liabilities and long-term debt denominated in foreign currencies are translated into Canadian dollars at the year-end rate; revenue and expenses are translated at rates in effect during the year.

Foreign exchange gains or loses arising on translation of long-term debt are deferred and amortized over the remaining terms of the debt. The amortization is included with interest. All other foreign exchange gains or losses are reflected in the consolidated statement of operations.

2. Status of Saskatchewan Mining Development Corporation

The Corporation was established by Order-in-Council #865/74 dated June 4, 1974 and continued under the Saskatchewan Mining Development Corporation Act, 1977. The Corporation's accounts are included in the annual consolidated statements of Crown Investments Corporation of Saskatchewan.

Saskatchewan Mining Development Corporation
December 31, 1986

3. Interest

	(thousands of dollars) 1986	1985
Interest		
on long-term debt	$ 71,027	$ 77,594
paid with concentrates	828	2,260
Amortization of deferred		
financing costs	1,287	1,081
foreign exchange gains and losses	11,289	13,676
	84,431	94,611
Less interest		
capitalized	28,309	24,156
earned	1,234	709
	29,543	24,865
	$ 54,888	$ 69,746

4. Inventories

	1986	1985
Broken ore and concentrates	$ 10,042	$ 9,504
Supplies	5,450	5,035
	$ 15,492	$ 14,539

5. Property, Plant and Equipment

	1986	1985
Producing properties		
Production facilities and equipment	$301,965	$299,916
Deferred mineral property costs	292,503	292,511
	594,468	592,427
Less accumulated depreciation and amortization	142,098	100,239
	452,370	492,188
Non-producing properties		
Exploration project areas	164,074	163,776
Key Lake Deilmann orebody	176,884	144,855
Cigar Lake	16,712	12,823
Star Lake	9,399	2,501
	367,069	323,955
	$819,439	$816,143
Property, Plant and Equipment includes interest capitalized		
During the year	$ 28,309	$ 24,156
Since inception	$275,851	$247,542

Saskatchewan Mining Development Corporation
December 31, 1986

6. Deferred Charges

	(thousands of dollars) 1986	1985
Deferred charges net of amortization consist of		
Gains and losses arising on translation of long-term debt	$ 22,634	$ 41,704
Financing costs	5,205	4,008
	$ 27,839	$ 45,712

7. Deferred Revenue

In 1986, the Corporation discharged its obligations under the terms of two uranium product loan agreements.

During the year the Corporation entered into an agreement which allows the Corporation to borrow gold bullion for periods agreed to by the Corporation and the lender. The agreement can be terminated by either party by giving 90 days written notice. The Corporation pays a monthly fee based upon the daily value of the gold bullion borrowed and upon an annual rate established by the parties every 180 days or at each loan renewal date. The loan is secured by a letter of credit guaranteed by the Province of Saskatchewan.

Pursuant to this agreement, the Corporation and the Cluff Mining partnership, under a separate agreement, borrowed bullion which was sold on the spot market. The proceeds, including the Corporation's share from the Cluff Mining partnership, amount to $9,339,000 and are included in deferred revenue. This deferred revenue will be included in earnings as gold bullion is returned to the respective lenders. Approximately one half of each of these borrowings will be returned during 1987.

Interest includes charges for borrowed concentrates and borrowed gold bullion.

8. Product Borrowed

Included in inventory are 193,518 lbs. of uranium concentrates which were borrowed in 1986. This inventory and the related liability are carried at cost of production. The Corporation will repay the loan by delivering to the lender an equivalent amount of uranium in the form of UF_6 during the period October 1, 1989 to December 31, 1991 and in lieu of interest, will pay a share of the cost of converting the uranium concentrates to UF_6. The loan is secured by a letter of credit guaranteed by the Province of Saskatchewan.

Saskatchewan Mining Development Corporation
December 31, 1986

9. Long-Term Debt

Province of Saskatchewan notes:

(thousands of dollars) Principal	Interest Rate	Maturity	(thousands of dollars) 1986	1985
$100,000 U.S.	16¼%	November 15, 1988 (subject to prior redemption)	$138,000	$139,830
77,663*	15⅜%	March 1, 1988	107,175	108,596
50,000	16 %	March 15, 1989	69,000	69,915
60,000	11⅞%	November 15, 1989	82,800	83,898
75,000	10¾%	March 15, 1990	103,500	104,872
35,000	8½%	March 5, 1991	48,300	—
25,000	7½%	July 24, 1991	34,500	—
$422,663 U.S.			$583,275	$507,111

*150 million Swiss francs hedged at $77,663 U.S.

The Corporation participates in several interest rate swap agreements which mature at various dates from August 1987 to September 1988. These agreements had the effect of converting $175,000,000 U.S. of fixed rate debt into floating rate debt. During the year, $35,000,000 U.S. of the floating rate swap portfolio was returned to a fixed rate obligation. The agreements include certain covenants on behalf of both parties to the agreements and provide for early termination of the agreements under specified conditions.

10. Province of Saskatchewan's Equity

Equity advances are non-interest bearing and are repayable at the discretion of the Province. Equity advances have been obtained from:

	(thousands of dollars) 1986	1985
The Saskatchewan Heritage Fund	$218,700	$218,700
Crown Investments Corporation of Saskatchewan	31,141	31,141
	$249,841	$249,841

Saskatchewan Mining Development Corporation
December 31, 1986

11. Commitments

The Corporation has financial commitments under various joint venture agreements it has entered into in the normal course of operations. The Corporation is required to pay its proportionate share of the exploration and development expenditures to maintain its interest in each joint venture.

12. Related Parties

Included in these financial statements are expense amounts resulting from routine operating transactions conducted at prevailing market prices with various Saskatchewan crown controlled departments, agencies and corporations with which the Corporation is related.

Account balances resulting from these transactions are included in the consolidated statement of financial position and are settled on normal trade terms.

Other amounts due to related parties and the terms of settlement are described separately in the consolidated financial statements and the notes thereto.

13. Remuneration of Directors and Senior Officers

The Corporation's eight directors (1985 — 8) received, in aggregate, $41,659 remuneration in 1986 (1985 — $28,500). Certain directors did not serve for the full year in 1985.

Fourteen senior officers (1985 — 16) received, in aggregate, $1,051,306 in salaries for 1986 (1985 — $1,230,114).

14. Segmented Information

a) Industry segment

The Corporation derives all of its sales revenue from the production and sale of uranium concentrates.

b) Sales of uranium concentrates

	(thousands of dollars)	
	1986	1985
Foreign	$174,118	$153,283
Domestic	5,823	21,270
	$179,941	$174,553

15. Comparative Figures

Certain comparative figures in the consolidated financial statements and notes thereto have been reclassified to conform to the current year's presentation.

HISTORIC FIVE YEAR REVIEW

	(thousands of dollars)				
	1986	1985	1984	1983	1982
Financial Position					
Total assets	$947,545	$898,169	$919,094	$812,985	$653,650
Total liabilities	663,716	629,732	660,706	562,235	403,799
Province's equity	283,829	268,437	258,388	250,750	249,851
Earnings					
Sales of concentrates	179,941	174,553	133,274	13,504	24,707
Operating earnings	85,280	87,795	60,940	2,099	5,496
Interest expense	54,888	69,746	45,702	—	—
Net earnings	30,392	18,049	15,238	2,099	5,496
Cash Flow					
From operations	109,166	100,757	50,546	14,206	13,608
Capital expenditures	24,079	21,020	28,266	124,820	130,696
Dividend to Province	15,000	8,000	7,600	1,200	1,200

DIRECTORS

MRS. HELEN SWAN
Mrs. Swan is a Saskatoon homemaker with a long-time record of community service. She is also an active member of the Corporation's Audit Committee.

HERBERT MORRISON
Mr. Morrison brings experience as both a banker and a stock broker; he is now a senior partner in a Saskatoon law firm. He serves on the Audit Committee for SMDC.

ALLAN BRIGDEN
Mr. Brigden is a resident of Kisbey, where he farms and operates a fertilizer, chemical and seed business. He is a member of the SMDC Compensation Committee.

JEROME GEDIR
Mr. Gedir owns and operates a financial and estate planning company in Prince Albert. He also serves as a member of the Audit Committee for the Corporation.

DR. SONJA RUSZNISKY
Dr. Rusznisky lives in Prince Albert, where she is a practicing psychologist and part owner of a bus company. She is actively involved on SMDC's Audit Committee.

MEL HEGLAND
Mr. Hegland is the mayor of La Ronge and part owner of a local airline. He is also a member of the Compensation Committee for SMDC.

WALTER NELSON
Mr. Nelson is involved in many business activities in and around the Avonlea area, and he is a member of SMDC's Compensation Committee.

Board members emerging from an underground tour of the Star Lake gold property in June, 1986. The Board later went on to visit the Cigar Lake uranium project.

From left to right: Dr. Sonya Rusznisky, Herbert Morrison, Allan Brigden, Mel Hegland, Walter Nelson, Mrs. Helen Swan, Jerome Gedir.

SMDC's Vice-Presidents review construction progress at the Star Lake site in the spring of 1986. By December, work had been completed ahead of schedule and under budget.

From left to right: John Tosney, Arnold Hillier, Dr. Gerald Pollock, Dr. Donald Somers, Jim Bonny.

VICE-PRESIDENTS

S.J. (JIM) BONNY
After spending several years in corporate planning and administration for another of Canada's major uranium producers, he joined SMDC in 1979 as Vice President, Marketing and Corporate Development.

ARNOLD E. HILLIER
Mr. Hillier has been the Vice President of Finance and Administration since joining the Corporation in 1980. He is also Corporate Secretary.

DR. GERALD D. POLLOCK
Dr. Pollock assumed the position of Vice President and General Manager of Exploration on January 1, 1985. Prior to this appointment, he had been employed at SMDC in a number of senior capacities in Exploration since 1974.

DR. DONALD G. SOMERS
Dr. Somers came to SMDC in 1981 in his present position of Vice President, Corporate Affairs. Prior to his appointment, he was involved in university research and was a consultant to a uranium development in northern Saskatchewan.

JOHN E. TOSNEY
Mr. Tosney came to SMDC in 1981 as Manager of Mining and Engineering. On January 1, 1985 he assumed his present position as Vice President and Manager, Mining and Engineering.